PHILIP MORRIS U.S.A.

INTER-OFFICE CORRESPONDENCE

Richmond, Virginia

To: **Mr. Larry Wexler** **Date: September 11, 1995**

From: **Audrey Dixon**

Subject: **Operations' Pro-Con Analysis of American Brands Production**

Attached is the pro-con analysis relative to our contract manufacturing the American Brands.

Currently the unanticipated growth in our export requirements, the trend to box product, and the conversion from 80 to 83mm product in the export markets creates uncertainty in demand, the need for additional capacity and stretches our resources to optimize the opportunities presented. The analysis to meet this export demand is still in progress.

The cons in the analysis relative to the American Brands reflect our concern over committing to additional volume in 1996. Our base production requirements for 1996 are 45 billion units greater than our production capability, requiring extensive use of overtime. Our export forecast may be understated and meeting actual volumes may require even greater use of overtime.

1996 is also a year that several projects will be underway to consolidate and increase capacity and reduce overtime. The analysis is based on assumptions related to equipment availability that results from current project plans and schedules. The assumption that the production of the American Brands could be phased in starting January, 1996 through March, 1997 is optimistic and is based on all other assumptions holding true.

Implementation of PM USA capacity projects during 1996 will require the same resources and disciplines needed to initiate production of the American Brands.

If there were a way to delay production of the American Brands to late-1996 or 1997, many of the cons would disappear and the pros could be realized, based on the current production forecast.

2072457675

Source: https://www.industrydocuments.ucsf.edu/docs/mqym0004

As I mentioned, the cost of producing the discount American Brands was based on using our Brica leaf blend. We are reevaluating the cost based on higher cost leaf blends. This information will be forwarded to you when available.

Operations' analysis of capacity is dynamic. Please let me know how I can provide additional input for this analysis.

CC: D. L. Milby

2072457676

Source: https://www.industrydocuments.ucsf.edu/docs/mqym0004

OPERATIONS' PRO-CON ANALYSIS OF THE CONTRACT MANUFACTURE OF AMERICAN BRANDS

PROS

- Provides additional, scheduled production given a downturn in requirements.
- Utilizes surplus soft-pack equipment (if equipment isn't used for conversion from X-1 to X-2).
- If additional volume of any kind is needed from Stockton Street, the fixed cost per thousand would be lowered by producing the volumes.
- These volumes could be met and still leave infrastructure at Stockton Street for 15 - 19 billion units of strategic reserve capacity.
- Overtime could be used to satisfy any additional surge requirements above the 15 - 19 billion units at Stockton Street.

CONS

- Accelerates the need for ET and BL capacity increases.
- Precludes 10 billion more units from being made for International.
- Utilizes equipment that could potentially go to PMI.
- Insufficient primary capacity at Stockton Street exists to produce American volumes, International requirements, Export Cut Filler and BBS. (cut filler could be shipped from the M/C to supplement Stockton's capacity without exceeding the M/C's primary capacity.)
- Production of American Brands in 1996 increases the risk of turning away business should demand exceed current volume projections.
- Introducing the American brands in 1996 further taxes support resources when approximately 45 billion units will be made on an overtime basis.

2072457677

Source: https://www.industrydocuments.ucsf.edu/docs/mqym0004

OPERATIONS' PRO-CON ANALYSIS OF THE CONTRACT MANUFACTURE OF AMERICAN BRANDS

The most current capacity scenario reflects the following annual cigarette production capacities at the four manufacturing facilities over the planned period. 1996 and 1997 requirements reflect July forecasts plus the additional volume represented by the American Brands. 1998 – 2000 requirements reflect additional business generated from available capacity plus additional volume represented by the American Brands.

(Billion Cigarettes)	1996	1997	1998	1999	2000
M/C	146.7	156.6	163.6	163.6	163.6
Cabarrus	109.0	146.0	163.0	165.0	165.0
Louisville	73.0	73.0	73.0	73.0	73.0
Stockton Street	20.0	16.0	13.0	13.0	13.0
TOTAL	348.7	391.6	412.6	414.6	414.6
Requirements Including American Brand Production	392.5	389.5	423.1	425.1	425.1

Stockton Street Scenario

- Transfer Parliament production to the M/C beginning in 1996 and continuing through 1997 for a net loss in cigarette manufacturing capacity of 20 billion units (10 billion in 96 & 10 billion in 97).
- Equipment installed at Stockton from 1996 through 1998 to provide International support will increase cigarette manufacturing capacity to 13 billion units (6 billion in 97 & 7 billion in 98).
- Stockton Street primary can support 56.2 billion units
- Maximum Make Pack Capacity existing infrastructure can support is 41 billion units
- Export Cut Filler requires approximately 7 billion units of cut filler annually
- Project Garden requires approximately 3 billion units of cut filler annually
- Equipment for the American Brands production requirements is made available in 1996 and 1997 from the M/C Capacity Consolidation project.

2072457678

SENT BY:Xerox Telecopier 7020 ; 9-12-95 ; 12:29 ; OPERATIONS MGT.→ 8121287821 65;# 5

Source: https://www.industrydocuments.ucsf.edu/docs/mqym0004

Stockton Street Manufacturing Options

(Billion Cigarettes)

Year	Total Primary Capacity	Total Mk/Pk Capacity Infrastructure will Support	Surplus Primary Capacity	ECF Requirements	Project Garden Requirements	Net Surplus Primary Capacity
1996	56.2	41.0	15.2	6.8	3.4	5.0
1997	56.2	41.0	15.2	6.2	3.4	5.6
1998	56.2	41.0	15.2	7.0	3.4	4.8
1999	56.2	41.0	15.2	7.1	3.4	4.9
2000	56.2	41.0	15.2	7.1*	3.4	4.9*

Year	Total Mk/Pk Capacity Infrastructure will Support	Installed Mk/Pk Capacity	Total Rqmt's.	Total Surplus Mk/Pk Capacity Infrastructure will Support	Total Surplus Primary Capacity	American Brand Capacity Rqmt's.	BBS Capacity Rqmt's.	Potential Mk/Pk Reserve Capacity	Strategic Mk/Pk Reserve Capacity with American Brands
1996	41.0	20.0	20.0	21.0	26.0	3.0	19.4	21.0	18.0
1997	41.0	16.0	16.0	25.0	30.6	10.0	40.7	25.0	15.0
1998	41.0	13.0	13.0	28.0	33.8	10.0	43.4	29.0	19.0
1999	41.0	13.0	13.0	28.0	33.9	10.0	44.0	29.0	19.0
2000	41.0	13.0	13.0	28.0	33.9*	10.0	44.6	29.0	19.0

* Note: Not available but assumed to be the same as the previous year

Source: https://www.industrydocuments.ucsf.edu/docs/mqym0004